

VZCZCXRO1827
RR RUEHCHI RUEHDT RUEHHM
DE RUEHJA #9864/01 2190015
ZNR UUUUU ZZH
R 070015Z AUG 06
FM AMEMBASSY JAKARTA
TO RUEHC/SECSTATE WASHDC 8332
RUCPDO/DEPT OF COMMERCE WASHDC
RHMFIUU/DEPT OF ENERGY WASHINGTON DC
RUEATRS/DEPT OF TREASURY WASHDC
INFO RUEHXS/ASSOCIATION OF SOUTHEAST ASIAN NATIONS
RUEHKO/AMEMBASSY TOKYO 9945
RUEHBY/AMEMBASSY CANBERRA 9792
RUEHBJ/AMEMBASSY BEIJING 3550

UNCLAS SECTION 01 OF 03 JAKARTA 009864

SIPDIS

DEPT FOR EAP/MTS, EB/IFD/OIA
DEPT PASS OPIC, EXIM, TDA
DOE FOR TOM CUTLER/PI-32 AND JANE NAKANO/PI-42
COMMERCE FOR USDOC 4430--GOLIKE
TREASURY FOR IA-SETH SEARLS

SENSITIVE
SIPDIS

E.O. 12958: N/A
TAGS: [ENRG](#) [ECON](#) [EINV](#) [SENV](#) [PGOV](#) [ID](#)
SUBJECT: GOI TO SPEND BILLIONS TO BOOST BIOFUELS

1. (U) SUMMARY: The Government of Indonesia (GOI) plans to invest USD 22 billion over the next five years to boost biofuel production in a bid to cut fossil fuel consumption. GOI officials say they will spend USD 6 billion to buy approximately 6 million hectares of land to grow the fuel feedstock. The remaining USD 16 billion will go toward building factories, roads and other support services. In January the GOI said it wanted to increase biofuel's share of the nation's fuel stock to ten percent. Sustained high global petroleum prices and the continued slow and steady decline of Indonesia's domestic production have given increased urgency toward greater use of alternative and renewable energy sources. Indonesian officials also want to promote employment in the agricultural sector as part of the President's initiative to cut unemployment and boost economic growth. Economists and environmentalists express reservations about the manner in which the GOI is seeking to boost biofuel production and increase energy security. End summary.

New Biofuel Initiative

2. (U) Minister of Energy and Mineral Resource Purnomo Yusgiantoro announced the GOI's biofuel initiative at a mid-July government conference on biofuels. He had promised that his ministry would release a biofuel master plan by the end of July with detailed financial incentives for small- and medium-sized companies to produce biofuel, as well as plans for regulatory relief to streamline the issuance of permits for large companies. During a 31 July meeting with industry representatives, however, ministry officials said the plan was still under development and could offer only the most general outlines of their initiative.

3. (U) Purnomo did not give concrete details but did say on July 31 that the Finance Ministry will formulate taxation and import duty incentives for biofuel production equipment. The Agriculture Ministry will seek ways to encourage raw materials production, while the Industry Ministry will be charged with streamlining plant licensing procedures, according to Purnomo. He said his ministry, Energy and Mineral Resources Ministry, will promulgate new guidelines on the types of biofuel to be sold. He also called on local governments to simplify the issuance of land use permits. Purnomo said the GOI has been conducting detailed

discussions with industry and internally within the government on the types of the incentives that will be made available.

14. (U) The Ministry did release interim biodiesel production targets through 2010: 187,000 kiloliters (KL) in 2007, 377,000 KL in 2008 and 1.337 million KL in 2010. So far in 2006 Indonesia has consumed a monthly average of 3.75 million KL of petroleum-based fuels or 45 million KL on an annual basis. Many analysts we have talked to say that the GOI has planned an extraordinarily ambitious program. By way of comparison, the United States, which began developing biofuel much earlier than Indonesia, produced only about 280,000 KL of biodiesel in 2005. American consumption of biofuel, including ethanol, accounts for three percent of U.S. total fuel demand.

15. (U) Biofuel can be produced from many different raw materials, including crude palm oil (CPO), sugar, and cassava, all of which are grown in abundance in Indonesia. CPO can be used to produce biodiesel, a replacement for diesel. Sugar and cassava can be used to produce bioethanol to replace gasoline. The GOI is also promoting the production of bio-oil, made from pure vegetable oil, and biogas, made of liquid waste and poultry droppings, both of which can be used as alternatives to kerosene. Some types of biofuel are already available in the retail marketplace, such as E-10, a combination of 10 percent ethanol and 90 percent gasoline, and B-10, a combination of 10 percent biodiesel and 90 percent diesel. Pertamina announced that effective August 1 it will cease selling unblended diesel in Jakarta.

JAKARTA 00009864 002 OF 003

16. (U) To kick off its campaign the GOI said initially on July 3 that it wanted to build a minimum of eight biofuel plants within the next few years using government funds. (Note: Later in the month, Purnomo used a figure of 11 plants. End Note.) Minister of Industry Fahmi Idris announced the plan after a cabinet meeting with President Susilo Bambang Yudhoyono in Magelang, Central Java. Fahmi said that four of the eight biofuel plants will have a production capacity of up to 7,000 KL a year while the other four will produce about 350 KL a year. All will use crude palm oil, cassava or castor oil as raw materials. He said that his ministry had not yet decided on the locations of the factories, but that they have offered the plan to all local administrations in the country. He said the determining factor will be proximity to plantations that can be used for feedstock. Construction will cost about about Rp 60 billion (US\$650,000) and will be financed from the 2006 national budget, according to Fahmi. The GOI plans to hand the facilities over to local administrations within a year of construction.

17. (U) Early in the year in January, the GOI issued President Instruction 1/2006 on Biofuel, which created the National Team for Biofuel Development, chaired by Al Hilal Hamdi, who was the Minister of Manpower in the Megawati administration. The team has the mandate to assist with the formulation of policies to accelerate biofuel development. Our energy ministry contacts tell us the government will also issue a Presidential Decree to support the operations of the team. The team met with President Susilo Bambang Yudhoyono (SBY) and several cabinet Ministers on July 1 and July 2 to discuss biofuel development and plan their strategy.

18. (U) SBY also held a limited cabinet meeting on July 24 to discuss biofuels. Our energy ministry contacts tell us that Coordinating Minister for the Economy Boediono and Coordinating Minister for People's Welfare Bakrie, as well the Ministers for Energy and Mineral Resource, State Owned Enterprises, Communication and Information, Finance, and Research and Technology attended. The directors of three

state owned banks, Mandiri, BNI, and BRI, also attended the meeting and they are expected to provide financing for biofuel development projects. The GOI is still yet to offer details on funding, but our sources say it will come at least partly come from a special budget for alternative energy which the Coordinating Minister for the Economy is creating.

New Policies and Financing

¶9. (U) On July 15, the GOI announced a plan to offer subsidized loans to palm oil, rubber and cacao plantations owners to expand their acreage cultivated, according to Bayu Krisnamurthi, a deputy at the Coordinating Ministry for the Economy, who announced the incentive scheme without providing further details. He explained that under the proposal, expected to come into force in the second half of 2006, a consortium of banks, led by Bank Rakyat Indonesia (BRI), will provide loans to the three sub-sectors at a fixed interest rate of 10 percent. The GOI will make up the difference between the fixed rate and the prevailing market rate through a subsidy payment to the banks. He also said that the GOI may allocate up to Rp 10 trillion (US\$ 1.1 billion) to subsidize increased lending to the plantation sector.

¶10. (U) During the 31 July meeting with industry representatives, Minister Purnomo said the GOI will need to issue new policies in five key areas: land supply, infrastructure, manufacturing, distribution, and financing. He said that the development of biofuels as an energy alternative to replace fossil fuel will also serve economic development and employment goals, too. He lauded the industry's potential to create jobs, saying it is expected to absorb 3.5 million in the workforce through 2010.

Biofuel Producers

JAKARTA 00009864 003 OF 003

¶11. (U) Even before the July announcements, four Indonesian companies had already said they will have biofuel plants up and running by the end of 2006. They include PT Sumiasih which is constructing a biofuel plant with an annual capacity of 70,000 KL. PT Sinar Mas is planning a facility with an annual capacity of 117,000 KL, as is PT Musimas. PT Mopoli has said it will build a plant with a capacity of 175,000 KL a year. The association of the Indonesian Oleochemical Producers (Apolin) chairman Kris Hadisubroto told reporters in June that the biodiesel plants will be located in Bekasi and Medan. He said that the total investment for the four plants will be around USD 25 million. They will use CPO as the raw material. Hadisubroto said the plants will cut into Indonesia's CPO exports, which he estimated would reach 12.5 million tons in 2006, but would not affect the country's overall CPO production. Indonesia is the world's second-largest palm oil producer and plans to develop another 9.0 million hectares (22.2 million acres) of plantations in the next five years, six million of which will be used to meet biofuel demand.

¶12. (U) Wilmar Holdings Ltd, a Singapore-based edible oil producer and refiner, said on July 3 that it will build a biodiesel plant to begin operations by 2007. The USD 20 million biodiesel plant in Riau will have an initial annual capacity of 250,000 tons with the potential for further expansion. Feedstock for this project will be mainly CPO, according to a Wilmar spokesman. Wilmar's plant will be racing to come on-stream ahead of a USD 25 million joint venture between plantation company PT Bakrie Sumatera Plantation and local construction firm PT Rekayasa Industri. Their plant is scheduled to begin operations in the middle of 2008 with an annual capacity between 60,000-100,000 tons.

¶13. (U) The GOI has also been looking for ways to collaborate with its neighbor and chief CPO competitor Malaysia. In a June 22 news conference, Indonesian and Malaysian state oil and gas companies Pertamina and Petronas said they will establish a joint research project to produce CPO-based biodiesel. Economic Coordinating Minister Boediono announced the plan for the Indonesians on the margins of a meeting between the leaders of the two neighboring countries.

Comment

¶14. (SBU) The push to ramp up biofuels use in Indonesia has significant implications for Indonesia's national energy security, agricultural sector employment, rural development, export revenue, and environmental protection. The costs of the many subsidies that the GOI says it intends to offer will be massive if they all come to fruition. A successful biofuels program will bring significant new employment in rural areas, perhaps millions of new jobs, according to the GOI, but at a significant cost to the treasury. At the same time, the plan calls for over six million hectares of land to be cleared. If not managed carefully, this may bode ill for Indonesia's already beleaguered biodiversity and alarming rates of deforestation. The GOI will also face significant challenges in running a massive land acquisition program without corruption. A Presidential advisor told us he was very worried about corruption related to the projects and was advising President Yudhoyono to proceed more cautiously. Given all the costs and uncertainties, it remains an open question whether Indonesia's energy security would be better served by continuing to phase out retail fuel subsidies, rather than embark on a heavily subsidized biofuel campaign.

PASCOE